App. F. IX-4

1949-50
(CB)

File No. 184-69

Previous References.

Serial Nos. 2

Later References.

GENERAL AND REVENUE SECRETARIAT

Serial Nos. one

Part B for Nov 49

SUBJECT

Agreements with the Government of Kerala - Option under Central Excise.

29/11

Agreements or Arrangements with the Govt of India etc

Central Excises:

With effect from 1-4-1950; the Central Excises come under the 'Federal List'. The following are the Excise Duties which come under the Pooling arrangements with the Govt of India under which both the Govt of India and Mysore share the proceeds of the duty levied within the State on the articles of consumption:

1. Excise Duty on Matches
2. Excise Duty on Sugar
3. Excise Duty on Betelnuts
4. Excise Duty on Coffee

5. Excise Duty on Tea.

6. Excise Duty on Tobacco

7. Excise Duty on Vegetable products

~~Excise Duty on Matches~~ :-

General :-

According to the existing constitution, Govt of India have no legal sanction to impose and collect Excise Duty on articles produced, grown, or manufactured within the States, so long as they are retained within the State.

When these ~~are~~ articles are imported into Indian territories, ~~it was~~ first in Indian State, not declared as foreign territory under Section 5 of the Indian

Tariff Act, 1894, it is open to the Govt of India to impose an import duty, equivalent to the excise duty, on the articles imported into British India from an Indian State.

The Govt of India suggested the desirability of the State levying a countervailing excise duty on sugar manufactured in Mysore.

Since 1934, the Govt are as a matter of policy levying from time to time, duty of Excises on certain articles at the rates fixed by the Govt of India. Certain reciprocal arrangements have been entered into with the Govt of India by which both the Govt of India and Mysore share the proceeds of such levy.

Policy on the subject was laid down by the Finance some time back. Mysore not really available at present.

The existing arrangements with the Govt of India are enumerated in respect of the items on ~~Ex~~ which Excise Duty is being levied:—

1. Excise Duty on Matches.

This was levied from April 1934 following a similar levy in India. According to the existing arrangement, the proceeds of the duty within the State are credited to the Govt of India and State gets a share of the total proceeds of the tax collected in the whole of India on an estimated consumption basis. In actual practice, the State retains the duty collected within the State & the Govt of India pay each year to the State, the difference

between the share creditable to the State on the estimated Population basis and the duty collected and retained in the State; the rate of levy of the Duty is in accordance with the rates levied by the Govt of India from time to time.

'Excise Duty on Sugar':—

This was introduced in the State for the first time in April 1934. upto 1940, the State was retaining the entire proceeds from the levy. According to the revised arrangement entered into with the Govt of India, since April 1940, the State has to pay the excess over the highest amount collected by the State in any of the previous years (Rs 12·91 lakhs collected during the year 1938-39)

to the Govt of India. As the duty collected during all the years (except the years 1940-41 & 1941-42) is below the prescribed limit, the whole proceeds of this levy are being retained by the State.

Excise Duty on Betelnuts :-

This has been abolished from 1-3-1948

Excise Duty on Coffee :-

This levy was introduced in the State with effect from 1-7-1944, as a defensive measure. Else the State would have lost the proceeds of this levy, which the Indian Govt would have imposed an Import Duty on all Coffee imported from Mysore into the Indian Territories. The distribution of the divisible proceeds and this levy between the Govt of India & Mysore is on consumption basis.

Excise Duty on Tea :-

The arrangement in this case is similar to the one existing in the case of coffee :- The revenue realised in the State ~~on this account of this levy~~ is retained up to the limit permissible on the basis of consumption; excess if any being credited to the Govt. of India.

Excise Duty on Tobacco :-

This duty was imposed with effect from 1-5-1943 following a similar levy in India.

Reference Vide Residency letter No D.F 69/43 genl. D 9-3-1943

According to the arrangement entered into with the Govt. of India in this behalf, the State is entitled to retain the proceeds of this duty subject to the a limit on the basis of the population of the State, which is in accordan

with the formula as indicated hereunder:-

$$A = \frac{P \times R}{P_1}$$

A Represents the limit retainable by the State

P = Population of the State

R = Total net revenue in any year (calculated from 1st April to the end of March of the year following) collected in India and all the participating States

Gross Revenue — Cost of collection

P_1

Excise Duty on Vegetable Products

The arrangement in this case is the same as the one in the case of Excise Duty on Tobacco.

Excise Duty on Superfine cloth

This is a new levy from March 1949

According to the existing

arrangement entered into

with the Govt of India,

distribution of the proceeds

between them the Govts is based

~~is based~~

on consumption, in the

case of Coffee, Tea, Tobacco

and Matches and Vegetable

products.

(b)

While in the case of Sugar,

collection in excess of Rs. 12.91/- lakhs

has to be credited to the Govt of

India

~~Sugar~~ X

On January 1948, the

Govt of India stated that the

existing arrangements in the matter

of sharing the proceeds of Excise Duties

levied in the State may continue

1500
CB

Agreement or Arrangement with the Govt of India for some time, pending a final settlement of the position under the new Constitution.

According to the terms of financial agreement recently entered into with the Govt of India, 'Excise Duties' form part of the Federal List, from 1-4-50, the States having no right to levy these duties or to share in the proceeds of such a levy.

In the absence of all the relevant materials on the subject, necessary information on the subject from the Explanatory Memorandum on the Budget for the year 1948-49 has been gathered. If approved, the above note may be got verified by a reference to the Rev Secy.

Chief Secy
14.10.49

Compiler
14/10

12/10/49

CHIEF SECRETARY 3528 14 OCT 1949 GOVT OF MYSORE

1993
UB

Agreements or Arrangements
With the Govt of India

A note received from the Excise Comm on the subject of Central Excise is placed below.

If approved, all these papers may be recorded.

B
Vs
10/11/09

10/11/09

Janab Mahomed Ismail Sheriff, B.A.,

1993

SRI K. SUBBA RAO, B.A.,
Excise Commissioner in Mysore.

NEW PUBLIC OFFICES,

Dated Bangalore, 31st Octr. 194 9.

D. O. No. Al-489/49.

Encls: Twelve.

URGENT.

Dear Sir,

With reference to your D.O.letter No.3756-68/C.P. dated 14th October 1949 requesting for copies of Agreements, Acts, Rules, etc., on the marginally noted subjects in respect of the arrangements existing between this Government and the Government of India, I write to enclose herewith, a brief Note indicating the working of these Acts in the State in accordance with the agreements entered into with the Government of India. All available references in this connection have been sent in original. I request that they may kindly be returned when done with.

* (1) Opium.
(2) Central Excises, Matches, Sugar, Tobacco, Coffee, Tea, Vegetable Oil Products, Betel-nut, Cotton cloth.

CB 32
5.11.49

Yours sincerely,

To

SRI K. SRINIVASAN, B.Sc.,
Chief Secretary to the Government of
H. H. The Maharaja of Mysore,
Bangalore.

Opium is to x
Regarding opium and central Excises, necessary notes have been sent separately.

The records may be returned to the Excise Comsr

A draft is put up

5/11/49

Issue xxxx
5/11/49
Issued as 5060/CB 58/11/49

(All these papers are not required in view of the fact that the Mysore Treaty of 1913 clearly states that 'Opium' is the exclusive property of the Govt of India.)

5/11/49

Dep

Janab Mahomed Ismail Sheriff, B.A.,

~~Mr. K. SUBBA RAO, B.A.,~~
Excise Commissioner,
Registrar of Associations and
Chief Conciliator in Mysore.

NEW PUBLIC OFFICES,

Dated Bangalore, 4th Novr. *194* 9.

D.O.No.Al-489/49.

Dear Sir,

With reference to your D.O.reminder dated 3rd November 1949 regarding Agreements, Acts, Rules, etc., relating to Opium and Central Excises, I write to state that a reply is being sent today with all the available references and information on the subject.

Yours sincerely,

To

Sri K. Srinivasan, B.Sc.,
Chief Secretary to the Government of
H.H.The Maharaja of Mysore, Bangalore.

Apparently the letters have crossed each other.

The connected papers on the subject (received from the Excise Comsr) have also been returned to the Excise Comsr

A NOTE ON REVENUE FROM EXCISE DUTIES.

When the Government of India decided early in 1934 to impose for the first time Excise Duties on Matches and Sugar - produced or manufactured in British India, they were at once confronted with a practical problem. There were a number of Indian States scattered all over Inida wherein these goods were being manufactured, and unless an effective arrangement were come to with the Governments of the States concerned, the producers of these goods would be able to send them into British India unburdened with any duty and compete at an undue advantage with the British Indian producers. The institution of a Custom's cordon round each such State, though theoritically possible, was not a feasible proposition. The non duty paid goods would still seep through the State boundary into the British Indian territory in a greater or lesser measure. The result would be a corresponding loss of Revenue to the Central Government. Besides, there was the real risk of many of the British Indian manufacturers shifting their operations into the adjacent Indian States with a view to escape the Excise Duty.

(2) To meet the above situation the Central Government armed themselves with power to impose an import duty equivalent to the Excise Duty on the relevant products imported into British India from an Indian State. At the same time, they decided not to exercise this power in respect of any State that consented to enact a corresponding law under which the Excise Duties in question would be levied in the State at the same rates and under the same conditions as in British India, from time to time. The entire revenue realised in British India and in the participating States would be pooled and shared on an agreed basis. Mysore was one of the first Indian States which consented to this arrangment which is even now in force.

(3) Excise Duty on Matches and Sugar.:- The Excise Duties on matches and Sugar came into force in Mysore with effect from 10-7-1934. The revenue realised from the duty on matches is shared on the population basis according to the formula $A = \frac{R \times T}{P}$

Where A = the share of Mysore State

R = Total net revenue in any year from 1st April till 31st March, collected in British India and all the participating States.

T = Population of the Mysore State.

P = Population of British India and all participating States.

The settlement on the population basis is not unfair so long as there is no import from foreign countries for internal consumption in India provided the average per capita consumption is roughly the same in all parts of India. The custom duties levied on such imports are not put into the pool but are appropriated wholly by the Government of India. In the case of matches, however, it is likely that all foreign imports - particularly from Sweeden, have ceased since 1940, and that the per capital consumption does not show much variation from Province to Province, so far as the Mysore State is concerned. Its production is much less than its consumption. In 1945-46 its share of revenue was about 9 lakhs out of which Rs.3 lakhs was collected as duty in the State.

(4) In the case of sugar the arrangement was somewhat different. Under the 1934 settlement the State was entitled to retain the entire revenue realised by the imposition of a countervailing excise duty. A revised arragnment came into force from 1-4-1940 under which the State agreed to hand over to the Government of India the excess over the highest amount collected in any of the previous years i.e., Rs.12.91 lakhs in 38-39. Small excess occurred in 40-41 and 41-42, and they were paid to the Central Government. But, in the subsequent years, the revenue realised has been less than this limit and consequently, no further payments have been made to the Govt. of India. The revenue for the current year as per revised estimate is 8.2 lakhs. I do not know why the existing arrangement has been characterised in the Secretariat note as crude and unfair to the State. I believe that the Sugar Factory at Mandya is producing more than the quantity required for internal consumption in the State and that an appreciable

portion of the manufacture is being exported into British India. If this is so, Mysore is now getting more than its share calculated on the basis of consumption. The question why Mysore should not be allowed to retain the whole of the proceeds without the restriction of an upper limit will be discussed later.

(5) Duties on Tobacco and Vegetable Product

India became involved in Second World War. The expenditure of the Central Government soon rose to abnormal heights. To meet this emergency the Government of India were compelled to impose excise duties on tobacco and on Vegetable Products with effect from 1-4-1943. Similar duties were imposed in Mysore from 1-5-1943. According to the agreement reached then the proceeds of the duties levied and realised in the State were to be shared on a proportional basis as per formula - $A = \frac{R \times T}{P}$

Where A = the amount retainable by the State out of the Excise revenue collected by the State.

R = total net revenue in any year from 1st April to 31st March collected in British India and all the participating States.

T = population of the State concerned.

P = population of British India and all participating States.

(6) This arrangement was to be in force for the duration of the War and one year thereafter i.e. till 31st March 1947. The first thing that strikes me about this arrangement is that it is much less favourable to the State than the agreement relating to the matches. If the net proceeds from these duties fell short of the amount calculated on the population basis it was to get nothing more. If on the otherhand, they exceeded that amount the surplus was payable to the Government of India. The exigency of war perhaps refrained our Government from pressing for a more equitable settlement.

(7) According to the Secretariat Note the net proceeds from the duty on tobacco have been less than the figures deduced according to the above formula in the years up to end of 1945-46. The calculation sheets for the subsequent years have not yet been received

from the Central Government and in their absence, it is not possible to say if there are any excesses payable to the Government of India. The position is expected to change radically when as a result of retrocession of the Civil Area, Bangalore, the Imperial Tobacco Factory situated there is taken over under the Mysore Government's administration. The application of the formula is likely to yield a heavy surplus in favour of the Central Government from the current year onwards and a controversy may develop over this issue.

(8) As regards Vegetable Products, it appears that the production in the State falls short of the consumption calculated on the population basis. Hence, it is not likely that any payment is due to the Central Government.

(9) Duties on betel-nuts, Coffee and Tea:- Consequent on the levy of Excise Duties in British India on betel-nuts, Coffee and Tea in the year 1944, the Mysore Government imposed similar duties on these products with effect from 14-8-1944. The formula suggested by the Government of India for sharing the proceeds was the same as that applicable to the distribution of revenue from the Tobacco and Vegetable Products Excise duties. The per capita consumption of tea in Mysore is perhaps less than the average for the whole of India. Tea habit in South India does not prevail to the same extent as in North India. But the case was otherwise as regards Coffee and betel-nuts, and it was not difficult to show that the adherence to the formula in these cases would be unfair to Mysore. Coffee was the drink of the South far excellence while very little of it was consumed up in the North. More over Mysore was the largest producer of Coffee and much of it which was of a higher quality than that produced in British India was exported outside India free of excise duty, and the duty levied on such exports

went to the coffers of the Central Government and not to the pool. The case of areca was similar. The Mysore production was considerable and of superior quality and a good proportion of it was consumed locally. India is not self sufficient as regards areca and cheaper qualities of this commodity are imported every year from the Far East. The custom duties levied on it are wholly appropriated by the Central Government. The Mysore Government therefore urged that the distribution of revenue in the case of Coffee and betl-nuts must be at least on the basis of consumption. It was agreed between the two Governments that the Mysore's share in the case of Coffee should be on the basis of consumption as exhibited in the statistics furnished by the Coffee Marketing Board. This arrangement was calculated to benefit the State, to the extent of 5 lakhs (from one lakh to 6 lakhs) As regards areca, it was estimated that the Mysore share would be Rs.3½ lakhs according to the formula and Rs.10 lakhs on the consumption basis. But the Government of India were unable to agree to share the revenue on the latter basis in the absence of reliable statistics as regards local consumption. It is however stated in the Secretariat Note that as a result of further discussion, it was agreed that the Central Government should take early steps to constitute the areca-nut Control Board on the model of the Coffee Board and that pending the establishment of that Board this Government should accpet the share on the population basis plus an arbitrary addition subject to the condition that allocation on the consumption basis would be worked out and given retropspective effect after the necessary statistics were collected by the Board. On the other hand, I find it stated the Residency letter No. R.F. 38-45/G & A dated 7th July 1945 t the Government of India after a careful study of the material supplied by the Mysore Government for sharing the revenue on t consumption basis came to the conclusion that the facts so adduced did not afford sufficient ground for adopting an al method of computation. It is likely that the Secretariat indicates the later stage of the negotiations between th ments. In the meanwhile the rate of duty on betel-nu

reduced from 2 annas to one anna per lb. from 1-4-1946 and subsequently the duty on areca nuts was wholly abolished - with effect from 29-2-1948. The question as to how and in what manner the revenue realised in the State during the period the duty on areca nuts was in force is to be shared still remains to be settled.

(10) The above arrangement regarding the sharing of - Excise duties between the Central Government and the participating states expired on March 31st, 1947. The subsequent developments and the arrangements now in force are indicated in the following letter No.F.12(4)-IB/47 dated 29th January 1948 from the Ministry of States, Government of India (copy enclosed). It is clearly stated in para 2 that the agreement of the States to the prolongation of the existing arrangements would be without prejudice to the financial benefit from April 1st, 1947, of any revised arrangements finally agreed to.

(11) I understand that the Mysore Government have since agreed to the above proposals and executed a Stand-still Agreement of which a copy has been furnished to me for reference. This Agreement reads as under :-

(Here reproduce the agreement) (enclosed).

" Central Excises " forms item 17 of the Schedule attached to the Agreement.

(12) It is against this background that one has to ...er the feasibility or otherwise of our obtaining a ...ion of the existing arrangements regarding the sharing ...e duties quite independently, and in advance of, ... of the much bigger problem of the future finan... the acceding States with the Central Govern... ...onstitution. It is even conceivable that ...ertain commodities may be classed as a ...ral taxation. A hint to this effect occurres

in the following passage of the Residency letter No. 2562/Legis. 49-33-1 dated 9th April 1934 :-

> I am therefore to explain that the arrangements now contemplated are not to be taken as producing the possible position of a sugar excise as a Federal source of revnue under a future constitution, but are to be regarded as a working arrangement which may be terminated by either party on reasonable notice if found not operating satisfactorily".

So long as the Stand-still Agreement is in force no such termination is of course now possible.

(13) The question is asked why a participating State should not be allowed to retian the entire proceeds from the levy of xcise Duties on the production or manufacture within its borders. This question has become one of great moment in view of the early possibility of the Imperial Tobacco Factory situated in the Civil Area coming under the jurisdiction of the Mysore Government. This Factory is stated to be owned by a British Company which has its headquarters at Calcutta. It holds a monopoly position and supplies almost the entire requirements of India as regards high or medium quality cigarettes. The production is stated to be of the order of 18 mellion cigarettes per day. In addition to the duty On tobacco used in the manufacture of a separ te duty on Cigarettes has been imposed with effect from 1st March 1948 and the annual revenue in the shape of duty om this one factory alone is now estimated at Rs. 4 crores. This tory imports some foreign tobacco for purposes of blending but the ncipal raw material used in the manufacture of Cigarettes is Virginia tobacco grown in India. The factory gets its major supply of tobacco from the Guntur Area, the State's contribution being limited to a small fraction of the total consumption on manufacture. Mysore consumes only a small fraction of the Factory's output. On the population basis the consumption may be between 2% and 3%. The factory is enabled to maintain its output at the present level because of the big free market in the rest of India which the existing agreement provides for its products. When once this market is closed the output is bound to fall to insignificant proportions. Under the

Under the existing arrangement the proceeds from the excise duties on tobacco and its products are Centrally pooled and shared according to the formula. As things stand the application of this formula may not bring in appreciable additional revenue to the coffers of the State even after the Factory comes under its administration. On the other hand the retention by the State of the entire revenue collected in the State would constitute a definite breach of the Standstill agreement. Apart from this, other consequences are likely to follow. In the event of a breach in the agreement the Central Government might choose to put Section 5 of the Central Excises and Salt Act 1944 into operation. That Section reads as follows:-

> " The Central Government may by notification in the official gazette, impose on any exciable goods other than salt brought into British India from the territory of any Indian state ..... a duty of customs equivalent to the duty imposed by this Act on the like goods produced or manufactured in British India".

The Excise duty on Cigarettes is a considerable proportion of the cost of manufacture and the Factory cannot possibly afford to pay double the duty - one duty in the State and another duty on export into British India. The British Indian consumer will have then to pay a much higher price than the Mysore consumer. In that event the owners of the Factory may be tempted to shift the site to the Guntur area in the Madras Province in an attempt to keep up production and escape the double levy, and in view of the high stakes involved, the Government of India may not be unwilling to facilitate the process of transfer by an offer of suitable compensation to the Factory.

CSV/-18-10-49.